

Accepted Manuscript

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PII: S1042-4431(17)30233-0

DOI: <http://dx.doi.org/10.1016/j.intfin.2017.05.008>

Reference: INTFIN 944

To appear in: *Journal of International Financial Markets, Institutions & Money*

Received Date: 13 May 2016

Accepted Date: 15 May 2017

Please cite this article as: A.M. Al-Awadhi, M. Dempsey, Social Norms and Market Outcomes: The Effects of Religious Beliefs on Stock Markets, *Journal of International Financial Markets, Institutions & Money* (2017), doi: <http://dx.doi.org/10.1016/j.intfin.2017.05.008>



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Abdullah M. Al-Awadhi², Michael Dempsey³

Abstract

This study investigates whether religious-based trading practices impede market development. As a natural experiment, we use data from the Gulf Cooperation Council (GCC) countries, which have clearly defined religious rules on investing in stock markets. We find that non-Islamic stocks in these markets are relatively neglected, have higher returns, lower liquidity, and face higher liquidity risk compared to Islamic stocks. Our overall evidence, therefore, supports the hypothesis of market segmentation. Our results highlight a potential challenge for the stock markets of religious Islamic societies in seeking to become globally competitive.

Keywords: Social norms; Market segmentation; Liquidity; Liquidity risk; Islamic stocks

¹The authors are grateful for helpful comments provided by the journal anonymous referees. We also express gratitude to the committee and the workshop participants at the KFUPM Islamic Banking and Finance Research Conference (2016). We are grateful to Vijaya B. Marisetty from RMIT University for his constructive comments that improved the paper.

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